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The Honorable Speaker and Members
House of Representatives of the State of Washington

Ladies and Gentlemen:

I am returning, without my approval as to Sections 124; 131(5); 204(1)(f); 205(2)(c); 205(2)(d); 211(6); 213(40); 213(44); 213(45); 213(49); 213(54); 302(13); 308, page 144, lines 27-28; 308(2); 308(12); 505(9); 511(18); 601(7); 714; 919; 925; 926; 930; and 935, Third Engrossed Substitute House Bill 2127 entitled:

“AN ACT Relating to fiscal matters.”

Section 124, page 18, Office of the State Treasurer, Supplemental Budget Reductions

The State Treasurer has made significant contributions to solving the state’s budget problem, including proposing a \$12.6 million transfer from the State Treasurer’s Service Account to the General Fund for my proposed 2012 supplemental operating budget. The Legislature increased this transfer to the General Fund by another \$3.5 million in Section 804 of this budget. This section would reduce appropriations to the Office of the State Treasurer by \$1.2 million. The Treasurer believes this 15 percent reduction would likely lead to lower investment earnings and higher risks to public funds. Moreover, this reduction in the Treasurer’s appropriation does not help the General Fund. Rather, it is the transfers in Section 804 that help the General Fund and this appropriation reduction was not included in the transfer. I am leaving Section 804 intact, but given the impacts that the appropriation reduction could have on timely administration of state finances, I am vetoing Section 124. The Treasurer has volunteered to place actual savings in reserve for a later transfer to the General Fund to help balance the next supplemental budget. For these reasons, I have vetoed Section 124.

Section 131(5), pages 32-34, Office of Financial Management, Office of Regulatory Assistance
Section 935, page 276, Office of Regulatory Assistance and Regulatory Agencies, Small Business Activities

The Office of Regulatory Assistance (ORA) is directed to coordinate an agency small business liaison team with regulatory agencies to recommend improvements to inspection practices and customer service. In addition, ORA must develop anonymous customer service surveys related to regulatory agencies and post them to its website. Similar activities were the subject of legislation that failed to pass the Legislature. The underlying goals of this proviso have already been incorporated into Executive Order 12-01, which directed ORA to establish a small business liaison

program, conduct regular outreach with small business groups to streamline and reduce redundancy in regulatory practices and inspections, and establish a web-based customer survey tool for input from all businesses. However, these legislative provisos also set prescriptive requirements on regulatory agencies to document inspection violations and corrective notices. These requirements should be established through a statutory change rather than the budget. In addition, insufficient funding is provided to ORA and regulatory agencies to implement these requirements. For these reasons, I have vetoed Section 131(5) and Section 935.

Section 204(1)(f), pages 60-61, Department of Social and Health Services, Jail Services Study

The Department of Social and Health Services is directed to submit a report to the Legislature by December 1, 2012, regarding the utilization of mental health services by those who are incarcerated or have been recently released from incarceration. No funding was provided to the Department to identify and compile the data necessary to compose the report by the deadline. For this reason, I have vetoed Section 204(1)(f).

Section 205(2)(c), pages 71-72, Department of Social and Health Services, Student Transition Funding

Funding is provided to the Department to contract with school districts for instructional support of new students with developmental disabilities that are admitted to a Residential Habilitation Center (RHC). This budget contains three mechanisms for school districts to obtain additional funding for providing special education services to students housed at RHCs, including one program based on demonstrated need for special education funding in excess of state and federal funding otherwise provided. Only one district would be eligible for this transition funding and it failed to demonstrate excessive costs related to special education for the 2011-12 school year. Because school districts have access to other fund sources when there is a demonstrated need, I have vetoed Section 205(2)(c).

Section 205(2)(d), page 72, Department of Social and Health Services, Rainier School Long-Range Development Plan

This proviso appropriates \$600,000 to create a long-range vision and development plan for Rainier School. Chapter 30, Laws of 2011 established a task force to make recommendations regarding the development of a system of services for persons with developmental disabilities and the state's long-term needs for residential habilitation center capacity. The long-range vision and development plan for Rainier School should be and is part of this larger, statewide strategy. For this reason, I have vetoed Section 205(2)(d).

Section 211(6), pages 87-88, Department of Social and Health Services, Funding for Community Initiative

The Department of Social and Health Services (DSHS) is required to maintain separate centralized administrative services for community health and safety networks that remain after the sunset of the Family Policy Council. DSHS has the administrative capacity to support this initiative within its current infrastructure. A separate administrative system within the Secretary's office is not necessary. For this reason, I have vetoed Section 211(6).

Section 213(40), page 103, Health Care Authority, Critical Access Hospitals

This proviso requires the Health Care Authority (HCA), in collaboration with numerous parties, to submit a design for rural health system access and quality incentive payments to the Legislature in December 2012. This represents a significant undertaking for which no funding is provided. However, the issue of how to use limited resources to best meet the health care needs of our state's

rural residents is an important one. I understand the Legislature intends to focus on this issue, and I will ask my staff and the staff of the relevant agencies to participate in and support these efforts. For this reason, I have vetoed Section 213(40).

Section 213(44), page 106, Health Care Authority, Facility Fees

This item directs the HCA to complete a study on the payment of facility fees and to issue a report to the Legislature by November 1, 2012. Both funding and time is insufficient for the successful completion of this study. Further, the Legislature passed Engrossed Substitute House Bill 2582 this past session which will require hospitals to report to the Department of Health a number of data requirements in regard to facility fees after January 1, 2013. It is premature to conduct this study until the necessary data are submitted and analyzed. For these reasons, I have vetoed Section 213(44).

Section 213(45), pages 106-107, Health Care Authority, Medicaid Managed Care

Section 213(45) requires the director of the HCA to make specific certifications of network adequacy to the Legislature and the Governor prior to awarding a contract for Medicaid managed care services. It also requires a rebidding process in counties where a certification cannot be established and prohibits a reversion to fee-for-service as a result of the procurement process. I am concerned that this proviso circumvents state laws requiring competitive procurements to be free from influence or bias. Competitive procurements ensure that public contracts are awarded based on quality and cost. The agency recently completed its procurement process for Medicaid managed care services. New competitors in the market were able to offer innovative proposals without sacrificing access or quality of care, saving taxpayers \$131 million in this biennium. This was done under the specific directive in this operating budget to “place substantial emphasis upon price competition in the selection of successful bidders,” when awarding managed care contracts for Medicaid enrollees. A federal judge recently upheld the competitive process. Unfortunately, some competitors did not compete on price, quality, and innovation criteria. This result is what we expect from a competitive procurement process. For these reasons, I have vetoed Section 213(45).

Section 213(49), page 108, Health Care Authority, Lowest Cost Generic Bidding

This proviso permits the HCA to enter into a competitive bidding process for the purchase of lowest cost generic drugs within the Medicaid program. The HCA already has the statutory authority to pursue competitive contracts through the Preferred Drug Program, and therefore, this proviso is not necessary. The current procurement model used by the agency has proven effective in obtaining the lowest cost generic on the market. Increased use of generic drugs has reduced Medicaid expenditures by \$118 million in the past five fiscal years. The model also is flexible in meeting the needs of patients and pharmacies by not limiting the choice of generic products and instead providing incentives for dispensing at the lowest cost. However, if another model were to prove more effective, current law gives the HCA the authority to move forward. For these reasons, I have vetoed Section 213(49).

Section 213(54), page 109, Health Care Authority, Rural Health Clinics

The HCA is directed to develop an alternative payment and reconciliation methodology for rural health clinics by December 1, 2012. This proviso is unnecessary as the HCA is committed to continuing discussions with the Rural Health Clinic Association of Washington and the Centers for Medicare and Medicaid Services to identify viable options for developing alternative payment and reconciliation methods. Groundwork was laid for this discussion with federal regulators last summer and fall, as the agency began exploratory discussions with the new federal Center for Medicare and Medicaid Innovation to gauge federal tolerance for innovation in this area. In

addition, too little time and money were provided to develop the study. For these reasons, I have vetoed Section 213(54).

Section 302(13), page 136, Department of Ecology, Implementation of Children's Safe Products Legislation

This proviso funds the Department of Ecology's responsibilities for implementing either Senate Bill 6120 or House Bill 2821, regarding children's safe products, with legislative direction that the appropriations would lapse if the bills were not enacted. These bills did not pass. For this reason, I have vetoed Section 302(13).

Section 308, page 144, lines 27-28, Department of Natural Resources, Fiscal Year 2013 General Fund-State Appropriation Change

Section 308(2), page 146, Department of Natural Resources, Emergency Fire Suppression

Section 925, page 268, Department of Natural Resources, Forest Development Account

Section 926, pages 268-269, Department of Natural Resources, Forest Development Account

Section 308(2) shifts \$2.1 million in fire suppression costs to the Forest Development Account, which is a trust management account used by the Department of Natural Resources (DNR) to pay for management of state forest trust lands that benefit 19 timber-dependent counties. It is not appropriate to require these 19 counties to bear the statewide costs of fire suppression, even partially, while other trusts and timber landowners remain unaffected. Additionally, \$623,000 in fire suppression overtime savings is assumed in this reduction, which is not feasible to achieve by DNR and its partners to manage wildfire responses. For these reasons, I have vetoed Section 308(2).

To restore funding sufficient to cover the \$2.1 million in fire suppression costs shifted back to the General Fund, I have also vetoed the fiscal year 2013 General Fund appropriation revision found in Section 308, page 144, lines 27-28. Because this veto will restore more funding than necessary to cover the fire suppression costs shifted back to General Fund-State, the Commissioner of Public Lands has agreed, at my request, to place \$1.2 million General Fund-State in reserve for fiscal year 2013.

Sections 925 and 926 make statutory changes needed to allow the use of the Forest Development Account for fire suppression costs by the Department of Natural Resources proposed in Section 308(2). Because I have vetoed Section 308(2), I have also vetoed Section 925 and Section 926.

Section 308(12), pages 148-149, Department of Natural Resources, Marina Rent Rates

Section 930, pages 272-273, Department of Natural Resources, Calculation of Annual Rent for Qualifying Marinas

These items have the effect of reducing marina rent solely benefiting two marinas in our state. Revising marina rent rates has long been an issue before the Legislature. The Department has completed several different studies and options for revising marina rents and introduced legislation as early as 2011 to implement these changes. These studies have clearly demonstrated that the current method to set marina rents is inequitable. The Legislature needs to take action on a permanent statutory change that addresses rents for all marinas within the state, not simply "pilot" a rent reduction for two marinas through the budget. Additionally, the lower rent rates would reduce revenue to the Aquatic Lands Enhancement Account by \$75,000 per year, an account which is already over-appropriated by \$2 million. For these reasons, I have vetoed Section 308(12) and Section 930.

Section 505(9), page 180, Office of the Superintendent of Public Instruction, Development of New Transportation Allocation Formula

The Office of the Superintendent of Public Instruction (OSPI) is required to develop a new state unit-cost pupil transportation funding allocation for schools, or a hybrid formula, for legislative consideration and potential adoption. From 2006 to 2011, the state invested more than \$1,000,000 to study and implement pupil transportation formula options. Consultants for the study, along with a working group of school district finance and transportation experts, recommended the expected cost model of funding over a unit-cost model. This model was enacted by the Legislature, effective September 1, 2011, and OSPI has proceeded with implementation. The state has carefully considered various formula options and invested considerable effort into developing the expected cost model. Another pupil transportation study is unwarranted. For these reasons, I have vetoed Section 505(9).

Section 511(18), page 192, Office of the Superintendent of Public Instruction, Education Reform Program, American Academy

This proviso allocates \$200,000 solely for The American Academy to provide social support and academic interventions to at-risk students. The American Academy is one of many programs in the state providing services to at-risk students. This proviso singles out a specific provider, The American Academy, for additional funding when other programs serving at-risk students are equally deserving. For this reason, I have vetoed Section 511(18).

Section 601(7), page 200, State Board for Community and Technical Colleges, Bellevue College Baccalaureate Degrees

Bellevue College would be temporarily authorized through this budget proviso to offer baccalaureate degrees, rather than applied baccalaureate degrees as currently authorized. The current applied baccalaureate pilot program at Bellevue College and other participating institutions shows promise. While expansion of baccalaureate degree programs into the state's community and technical college system may ultimately prove to be sound public policy, such authorization through a budget proviso is the wrong approach. The Legislature endorsed the System Design Plan in 2010 for the purpose of establishing a process for the expansion of new programs and degrees where there is demand and to ensure financial sustainability. This important planning process cannot succeed if independent authorization is given in a budget proviso. Moreover, it is unlikely that implementation of degree programs on a new campus can be completed by June 30, 2013, when the authority in this subsection will expire. For these reasons, I have vetoed Section 601(7).

Section 714, pages 232-233, Office of Financial Management, Fiscal Year 2013 Information Technology Savings

Section 714 directs the Office of Financial Management to identify information technology (IT) savings and to reduce state agency allotments by \$10 million in all funds. The 2011-13 budget already includes another \$60 million in central service reductions, as well as administrative cuts in multiple agencies and the expectation that agencies will under-spend their revised budgets by \$120 million of reversions. While the state will continue to pursue savings in IT and other back office functions, we have to be realistic about the detrimental effect of random reduction targets. At some point, agencies will not be able to deliver expected services even with increased productivity. So, enough is enough. For this reason, I have vetoed Section 714.

Section 919, pages 253-257, Office of the Governor, Across-the-Board Reductions

Existing law gives the Governor authority to impose across-the-board spending reductions when a cash deficit is projected in a particular fund. To prevent the necessity of a special session if

revenues decline, I asked the Legislature for more flexibility in the event there was a need to reduce State General Fund expenditure authority. However, this language actually reduces executive flexibility by mandating that all provisoed amounts be reduced by the same percentage as separate appropriations. While agencies must respect legislative priorities when implementing across-the-board reductions, mandating the preservation of provisoed funds over core services is the wrong approach. For these reasons, I have vetoed Section 919.

I am not vetoing Section 307, which transfers \$3.3 million of the Department of Fish and Wildlife's enforcement expenses from the State General Fund to the Recreation Resources Account. However, I do have concerns about this provision of the bill. A veto would not restore the \$3.3 million General Fund reduction and would result in the elimination of 30 enforcement officer positions. The Department cannot effectively enforce state fish and wildlife regulations with a reduction of this magnitude. The Recreation Resources Account provides grants for local boating projects across the state. The Legislature should reconsider this transfer next session.

With the exception of Sections 124; 131(5); 204(1)(f); 205(2)(c); 205(2)(d); 211(6); 213(40); 213(44); 213(45); 213(49); 213(54); 302(13); 308, page 144, lines 27-28; 308(2); 308(12); 505(9); 511(18); 601(7); 714; 919; 925; 926; 930; and 935, Third Engrossed Substitute House Bill 2127 is approved.

Respectfully submitted,

Christine Gregoire
Governor